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# Political Economy Analysis of Local Economic Development in Serbia

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## Disclaimer

This report has been produced by IDS and Marija Žikić. The views expressed in the report do not necessarily represent those of the Swiss Agency for Development and Cooperation.

# 1 Introduction

Local Economic Development (LED) has gained renewed interest within SDC and beyond. In particular, there has been greater recognition of the importance and role of a functioning local government system in implementing successful local economic development interventions that can generate employment and income in all parts of the country, and especially in less developed, more marginalised regions. This study uses a political economy lens to analyse the challenge of strengthening LED offices in local self-government units so that they can facilitate and support local economic development in Serbia that can:

- Improve the competitiveness of micro enterprises (MEs — small businesses with up to ten employees), especially in rural municipalities that are more remote and less developed, and more likely to fall outside the net of national activities;
- Reduce unemployment and de-population in these municipalities;
- Increase economic opportunities in particular for women, youth, and the residents of rural and less developed municipalities.

## 1.1. Background and context

Support to local economic development is an important responsibility of local self-government units in Serbia, and is focused mainly on their facilitation of micro, small and medium-sized local businesses (SMEs). According to a 2017 report on SMEs by the Ministry of Economy<sup>1</sup>, there are 357,234 registered SMEs in Serbia, which generate 1,325.7 billion RSD in gross value (€10.9 billion) and employ 873,462 workers. This sector accounts for 66 per cent of total employment, 56.7 per cent of gross value added and 39.5 per cent of non-financial sector exports. The largest number of SMEs are concentrated in three sectors: trade (27.2 per cent), manufacturing (15.5 per cent), and professional services (12.6 per cent).

But Serbia is a country of great regional differences, and there are large territorial differentials in the level of development of the SME sector — dominated by the Belgrade region and with districts like Toplica, Pirot and Zaječar lying at the other end of the spectrum, together accounting for only 2.6 per cent of the total number of SMEs, and which employ 2.8 per cent of workers and generate 1.8 per cent of GDP of the total SME sector. The competitiveness of the SME sector in Serbia is quite low, and lags significantly in comparison to the EU-28 average — SMEs in Serbia in 2016 employed an average of 2.5 workers per enterprise (EU-28 average of four workers), and their productivity was 3.7 times lower than the EU-28 average. Within Serbia, SMEs from the Belgrade region are twice as productive as those from South and East Serbia, 1.7 times as productive as those from Šumadija and Western Serbia, and 1.3 times in relation to SMEs from Vojvodina.<sup>2</sup>

Serbia's economic growth has been concentrated in larger cities, while the highest unemployment rates and poverty levels are recorded in the smaller towns and rural

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<sup>1</sup> Report on small and medium enterprises and entrepreneurship 2017, Ministry of Economy, November 2018, [http://privreda.gov.rs/wp-content/uploads/2019/01/Izvestaj\\_MSPP\\_2017.pdf](http://privreda.gov.rs/wp-content/uploads/2019/01/Izvestaj_MSPP_2017.pdf)

<sup>2</sup> Milorad, Filipović, Nikolić Miroljub and Cvetanović Slobodan, 2015, 'Razvoj preduzetničkog sektora kao osnove jačanja konkurentnosti privrede', *Ekonomika preduzeća*, Vol. 63(3-4), pg. 205-221

communities. In parallel to this, and partially as a consequence, there is a strong internal migratory trend towards big cities like Belgrade, Novi sad, and Niš. Unemployment in Serbia is high at 12.9 per cent,<sup>3</sup> with the highest unemployment in South and East Serbia at 15.9 per cent, or in the region of Šumadija and Western Serbia at 14.8 per cent. Together with this, there is also a high level of de-population of the countryside and smaller towns. This trend makes small communities less competitive, both economically and socially. Lack of adequate living standards and social infrastructure is deterring young people and an educated labour force from staying in small and rural communities.

According to the 2017 SMEs Report, investments in the SME sector decreased by 19.1 per cent over a ten-year period. The global economic crisis of 2008 is one reason for this, but an equally important reason is the lack of state support for this sector. Support to SMEs is the function of LED offices within local self-governments, and over the past ten years, most local self-governments in Serbia have been galvanised to do everything in their power to attract more direct investments in order to create new jobs and increase living standards of their population. However, some municipalities are more successful in this process than others.

The establishment and functioning of LED offices across Serbia is the result of various donor programmes over the period 2006-2012, such as MEGA (Municipal Economic Growth Activity – USAID), local economy development in Eastern Serbia (GIZ), and others. The 2015 Law on Investments made LED offices mandatory in each municipality (or group of municipalities), naming it Unit for Local Economic Development and Investment Support (Articles 15, 19 and 20). LED units in local self-governments are differently founded — most of them are part of the local administration and are formed as departments or divisions of local self-government, while a few have been established as separate legal entities. They also have differential capacity, and depending on this, they have differing functions and their staff numbers can range from just one to over 30. The scope of their activities involves investment promotion, monitoring local labour markets, mapping and presenting investment locations within the boundaries of local self-governments, support to SMEs, and the implementation and monitoring of municipal economic development strategies. The development of communal and local economic infrastructure is the regular responsibility of all LED offices, primarily through project writing and fund raising. Staff in LED offices mainly prepare projects for all kinds of public calls that are addressed to local governments, from infrastructure to social projects. This requires different and specific knowledge and expertise, which is not always present within LED offices.

This study is centrally concerned with a political economy analysis of the multiple challenges involved in LED offices within local self-governments being able to successfully promote, support and implement local economic development.

## **1.2. Cases and Method**

The analysis and findings presented in this study are based on semi-structured interviews conducted with a range of actors from local government and the private sector in six municipalities in Serbia. The six case municipalities were selected through a consultative

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<sup>3</sup> Statistical Office of the Republic of Serbia, <http://www.stat.gov.rs/sr-latn/vesti/20180228-anketa-o-radnoj-snazi-4kv-2018/?s=2400>

process from an initial listing of representative municipalities across different regions provided by the Standing Conference on Towns and Municipalities (SCTM) to the SCO Serbia office. These were considered representative in terms of levels of development, and types of issues faced by a majority of municipalities. From this list, we selected municipalities to represent each of the five development groups across which local self-governments (LSGs) in Serbia are divided. These groups are the following:

- Group I — Developed, more than Republic average – Includes 20 LSGs
- Group II — Developed, 80-100 per cent of Republic average – Includes 34 LSGs
- Group III — Underdeveloped, 60-80 per cent of Republic average – Includes 47 LSGs
- Group IV — Extremely underdeveloped, under 60 per cent of Republic average – Includes 44 LSGs
- Devastated areas — Under 50 per cent of Republic average – Includes 19 LSGs

Another criteria used for case selection was the size of the municipality, in order to ensure that we were able to capture issues of relevance to different types of local self-governments. This gave us the following six municipalities:

	Less Developed	More Developed
Small	<b>Bojnik (Devastated)</b> <b>Aleksinac (Group IV)</b>	<b>Trstenik (Group III)</b>
Large	<b>Leskovac (Group III)</b>	<b>Kruševac (Group II)</b> <b>Niš (Group I)</b>

Information for the analysis was collected largely through semi-structured in-depth interviews in these municipalities. A detailed list of questions was prepared for interviews with different types of actors — municipal staff in LED offices; private sector actors; RDAs; and a list of national level institutions (the full list of interviews is attached in Annex 1). However, most interviews were conducted as free flowing conversations, prompted with the prepared list of questions when required, in order to ensure more open conversations that could get at the foundations of the main challenges faced by local staff in implementing LED. A short note on the municipality of Sokobanja was also prepared in order to draw on the local expertise and experiences of the local consultant involved in this study.

### 1.3. Organisation of the study

This study is organised as follows: Section 2 provides the political economy analysis of the role of local governments in promoting and supporting local economic development in Serbia. The section is organised across four sections — structural factors; power dynamics; actors interests and incentives; and the drivers and constrainers of change. Each sub-section highlights the main challenges that emanate from each set of factors and ends with a set of plausible solutions that could help mitigate these challenges. Section 3 then connects these solutions to specific interventions that can be designed to implement these. Across the next two sections, therefore, this study uses a political economy lens to move all the way from identified challenges to their solutions and some possible suggested interventions.

## 2 Political Economy Analysis

Political Economy Analysis (PEA) is a methodology that allows us to examine the impact of the interaction between relevant dimensions of the socio-economic and political structure; power dynamics and the rules of the game; interests and incentives of the key actors; and the main drivers and constrainers of change. The aim of this analysis is to examine the contextual factors that condition the state of affairs in a given issue area — in this case, the role of local self-governments in implementing successful local economic development — and to identify the areas in which change is possible, and can be induced through custom-designed interventions.

Drawing on the PEA methodology used by Hempfling *et al.*'s (2016)<sup>4</sup> report on competitiveness in Serbia, and combining this with a particular focus on power dynamics and drivers of change, this analysis is organised around the following four main sections: foundational or structural factors; rules of the game and the dynamics of power; actor interests and incentives; and the main drivers and constrainers of change. Each section below is divided across the main challenges within this area, and the possible, feasible ways in which these can be addressed.

### 2.1. Structural Factors

In terms of foundational structural factors that are affecting the issue of local economic development and the role of local self-governments in implementing this, a few of the most prominent are the following.

#### *Informal centralisation despite formal decentralisation*

The most central factor is possibly the structure and nature of local government in Serbia. To put it simply, despite a good level of decentralisation, governance is actually quite centralised. This is paradoxical but emanates from the fact that while a system of autonomous local self-governments exists across all parts of the country, directives flow largely from the centre and there is restricted budgetary space for decision-making at the local level. Respondents pointed out that such centralisation is real and pervasive, but actually informal — while local self-governments are formally autonomous, there has been an informal process of centralising authority in the centre which works through the issuance of directives and through political alliances that look to the centre to set local priorities.

The establishment and functioning of local self-government units in Serbia is defined by the Law on Local Self-Government (Official Gazette of Republic of Serbia no. 129/2007, 83/2014, 101/2016 and 47/2018). The law suggests that in the exercise of their responsibilities, local self-government units can pass regulations independently, in accordance with their rights and obligations determined by the constitution, the law, and other regulations and statutes. Despite this provision, the units of local self-government are

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<sup>4</sup> Hempfling, Craig, Richard Danicic, Edi Majstorovic and Branislav Savic. 2016. 'Serbia Competitiveness Assessment and Political Economy Analysis', Report No. 29, Leveraging Economic Opportunities (LEO) project, United States Agency for International Development.

not completely independent in the exercise of their competences because most of the tasks they perform require the approval of central ministries. The most stringent of these are the annual instructions and frameworks they receive from the Ministry of Finance for creating local budgets.

Another relevant aspect of decentralisation in Serbia is the fact that the law divides the country into a single tier of decentralised government based on monotype municipalities. Our respondents in this study, as well as an earlier one conducted for SDC<sup>5</sup>, pointed out that the implementation of these laws did not account for demographic, financial and resource differences between municipalities and, instead, devolved uniform competences to each one regardless of size, resources or type. This uniformity has had two results. Firstly, that rural, small, remote and poorly endowed municipalities are expected to perform the same set of 15 functions and take on the same responsibilities as larger, better endowed municipalities that are closer to urban areas (the responsibilities of city municipalities are defined differently). Secondly, all municipalities are expected to perform the same tasks and take on similar responsibilities regardless of their actual capacity for these tasks. To put it starkly, an urban municipality in Belgrade has almost the same responsibilities as a remote, rural municipality in the south of Serbia. A number of respondents pointed out that this 'one size fits all' system has created inefficiencies and limited some municipalities in their ability to deliver services effectively.

Central directives issued by ministries to a uniformly designed set of local self-governments means that national regulations and instructions are rarely designed with the specific needs of different municipalities in mind. Small and remote municipalities are usually the ones that lose out in the process, tasked as they are with delivering functions that are designed with larger and better resourced municipalities in mind. One respondent pointed out that 'national institutions will affect as much of the country as possible, without thinking much of specific local needs. Local level must develop their own instruments for their needs'. But when it comes to LED, smaller local self-governments have few guidelines on how to do this. This is discussed in Section 2.2.

### *Lack of institutional coherence*

The situation defined above leads to a level of institutional incoherence that was pointed out by a number of respondents — local governments are uniformly defined and implemented across the country, yet they are centrally directed, but with vaguely defined guidelines for the many and quite complex tasks that municipalities must take on. One of the consequences of this configuration is that while local governments require support (rather than direction), central ministries use the formal autonomy of municipalities to deflect responsibility. We heard from relevant ministries at the centre that they were not responsible for the lack of performance on LED at the local level because local self-governments were 'autonomous', 'that they were responsible for everything', and that the centre did not want to 'be issuing directives'.

Serbia has many institutions, agencies and regulatory frameworks across different tiers of government, and has the kind of 'institutional thickness' often suggested as a necessary

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<sup>5</sup> Khan Mohmand, Shandana and Dušan Pavlović. 2013. 'Political Economy of Decentralisation in Serbia', Mimeo, SDC.



prerequisite for strong governance. However, many respondents at all levels pointed out that these institutions and regulatory frameworks lack coherence, in that they do not work towards common goals that are defined by unified and shared objectives. This creates a system that is characterised by both gaps and overlaps — the work of local, regional, and national institutions, private sector actors, and donors often focus on similar areas to create overlaps in one issue space, which leaves gaps in other issue spaces that receive less attention. This, pointed out a respondent in a ministry, often happens around particularly ‘trendy issues’, such as supply and value chains at the moment in Serbia. There is the need to ensure that different institutions and actors coordinate their work in moving towards common goals by providing different but complementary functions. As one respondent put it, ‘everything has been initiated, the various pieces of the puzzle all exist, they all now need to be put together’.

These trends have two distinct implications for the issue of LED. First, that local and national institutions are ‘passing the buck’ between each other in terms of pinning the responsibility for a lack of performance on the other actor. National institutions insist that municipalities are autonomous and therefore responsible for the current state of affairs, while municipalities point out that they receive many directives but few guidelines or resources to guide their work in this area. Second, LED as an issue seems to have ‘fallen through the cracks’ and got lost in the lack of coordination between ministries. Officials in the municipalities we visited insisted that they needed the support of central ministries on the issue of LED, especially the ministries of Economy and of Public Administration and Local Self-Government, but both ministries insisted that LED was not an issue that fell within their jurisdiction and referred us to the other ministry as the main stakeholder.

### *Lack of practical knowledge in workforce*

On the other side of the equation, various respondents pointed out that the workforce lacks skills and practical knowledge valued by businesses. This is connected to a lack of vocational training and ‘dual-education’ programmes that can provide local populations with the type of skills sought out by investors. There are some local programmes focused on this, and there was evidence that this is becoming an area of growing attention for both central and local actors. But for now, it does provide a key constraint in this area.

### *Solutions*

Foundational, structural factors are almost always difficult to address because they require a systemic push for change from within the system. For LED, this is missing at the moment — there is no pressure for change from within, and there is limited space for achieving such change from outside. A few suggested solutions fall within this limited space:

- Integrated planning and vertical linkages: Develop capacity for flexible, but functional, planning at the local level that is customised to the needs of the local economy and businesses. Together with capacity, create incentives for the development of ‘local development plans’ that can integrate the work of different ministries, agencies and donors, and direct these towards locally identified, common economic objectives for the region.
- Guidelines: Develop central guidelines that can provide support to local planning staff

through tools, tips, and more details on specific functions that can support local businesses, without getting prescriptive. Greater clarity is required in particular on local and national frameworks that can create a more adaptive and supportive environment for local micro enterprises (MEs).

- Inter-municipal cooperation: Incentivise inter-municipal cooperation to bring two or more municipalities together in developing common local economic programmes and development plans. Almost all respondents emphasised this as a key solution to the lack of capacity, expertise, staff and resources for LED at the local level, and to creating more coherent, horizontally and vertically integrated local development plans.
- Inter-ministerial cooperation: Advocate for and incentivise the creation of inter-ministry groups on LED at the national level that can create greater horizontal coherence for work in this area.

## 2.2. Rules of the Game and Power Dynamics

In terms of the rules of the game and the power dynamics at play within the system, the most prominent aspects include the following:

### *Recent and limited legal base for LED*

While the system of local governance is uniformly applied across the country — regardless of the size of the municipality or the state of local capacity — laws on local economic development are under-defined and vague. Together, this creates large gaps in how LED is implemented at the local level. Many smaller municipalities do not have the capacity to perform their defined roles in the same way as larger municipalities, and this situation is worsened when the legal guidelines provided for activities such as LED are limited.

Local self-governments in Serbia gained the jurisdiction over local economic development activities after the adoption of the new Law on Local Self-Government in 2007, and became the last country in the Western Balkan region that shifted this competence from the central to the local level. Two laws regulate this area: The Law on Local Self-Government and the Law on Investments (Official Gazette of the Republic of Serbia, No. 89/2015 and 95/2018).

The Law on Local Self-Government defines the jurisdiction of local self-governments on LED in a single line of Article 20, paragraph 7, which says that the LSG jurisdiction in the field of local economic development is to:

- adopt and implement programmes to encourage local economic development,
- undertake activities to maintain existing and attract new investments, and
- improve general business conditions.

The provisions of these laws on governing the subject of LED are thus very brief and leave a lot of room for flexible interpretation. Many of our respondents believe that this has led to a number of issues. Firstly, there is a lack of clarity within municipalities on what is expected of them on LED. Secondly, it has contributed to a lack of capacity on LED at the local level. And thirdly, this is a major reason as to why the functions of LED offices vary significantly across different municipalities, and why citizens and businesses receive variable levels and quality of services across different parts of the country.

The Law on Investments is equally brief and vague on this area. The law regulates the general legal framework for investments in Serbia and defines the entities and institutions for supporting investments and the efficient provision of services to investors. According to this law, the unit for local economic development and investment support is the organisational part of a local self-government unit or a legal entity that provides professional assistance and support to investors. It does not insist on the mandatory establishment of a unit for local economic development, and different municipalities can come up with different arrangements for dealing with this. While flexibility can be useful in designing contextualised local interventions, a lack of clarity in the regulatory framework in this case has resulted in variable quality of services across the country, and in LED offices becoming 'catch-all' spaces for activities that do not neatly fall into other local departments.

Lack of supportive guidelines leads to a lack of expertise, even where laws are clearer. For instance, while the law provides for local economic programmes that can subsidise local businesses not only financially but also in kind through, for example, the provision of business premises free of charge, only six local self-governments have instituted such a programme at present. The main constraint is that municipalities do not have the requisite knowledge or expertise to make use of the various subsidies and support mechanisms provided for in the law to create enabling environments for local businesses.

Two other regulations adopted in 2018 are expected to significantly impact the functioning of LED offices. The first is the Law on Planning System (Official Gazette of the Republic of Serbia, No. 30/2018) that regulates the content and management of development plans for public policies, compliance with such planning documents, the procedure for their implementation, and the evaluation of the impact of public policies. This law has the potential to introduce exactly the type of vertically integrated development planning discussed in the previous section, bringing together national and local actors in planning public policy. Article 9 of the law prescribes a development plan of the local self-government unit that sets out an integrated strategy for at least seven years. The development plan must contain an overview and analysis of the current situation, a vision, the priority development goals, as well as an overview and a brief description of the appropriate measures that are further elaborated by the public policy documents and the mid-term plans (valid for three years) of the local self-government unit. Significantly, this law has the potential to closely align local budgets with the development plans, thus restricting the current practice of ad hoc budgetary allocations that many respondents said are politically motivated, damaging to planning processes, and lead to the wasteful use of limited resources. This will of course require scrutiny and sanctions to ensure compliance by the state audit institution, an announcement that has already been made. Some respondents pointed out, however, that the law is very complex with far too many by-laws and not enough guidelines on how to implement it, so that municipalities will possibly require external support in dealing with it.

The other is the Regulation on content, manner of preparation and evaluation, as well as monitoring of implementation and reporting on realisation of capital projects (Official Gazette of the Republic of Serbia, number 63/2017). This regulates the evaluation of the implementation of capital projects, emphasising the need to better monitor, document and analyse the effects of such projects.

Implemented well, both these new laws have the potential to provide better guidance to local

self-governments, and specifically to LED offices within these, on successfully implementing local economic development, and increasing their ability for more integrated planning to achieve these aims, by outlining in more detail the selection and management of capital projects, in line with priorities identified in local development plans that are formulated in local legislative assemblies.

### *Politics of patronage*

The fact that the Serbian bureaucracy functions through very high levels of political patronage was pointed out by almost all respondents at all levels. This refers to the fact that appointments within the public service at both the national and local levels are often politically motivated. The most relevant impact of this for our purpose here is that it reduces capacity within local self-governments in general, and within LED offices in particular, which function as catch-all spaces despite the fact that a high level of expertise is required within these. Political appointees with little technical expertise on the issue or knowledge of the laws and regulations may often be placed to make decisions in quite technical areas, leading to poor implementation. This also weakens the ability of municipalities to formulate and implement integrated plans, given that many decisions and budgetary allocations may be politically motivated.

Furthermore, the fact that political changes at the national level impact political coalitions at all levels means that there are frequent changes at the local level. This, coupled with the fact that political parties appoint their own people to key positions, means that there is little permanence in terms of staff or capacity. While the laws listed above aim to deal with strengthening systems of planning, it is easy to see that much also depends on regulations that can deal with reducing the prevalence of patronage politics within the Serbian public service. As one respondent pointed out, 'things don't settle down. There are changes in all departments. People come and go because of high staff turnover, but also because of politics. There are political appointments even in technical services, such as agricultural advisory services'. The lack of staff continuity leads to a lack of continuity in structures and capacities within decentralised units, leaving little space for long term thinking or planning.

Another impact of the politics of patronage is unequal development. Local self-governments of the ruling party have a strong connection to the national level, which translates into greater political support for them vis-à-vis local self-governments led by opposition parties, as well as the possibility of more resources and more favourable conditions in which to implement programmes. Respondents in ministries at the national level confirmed this in pointing out that most vertical linkages between the centre and municipalities functioned through political channels within parties, rather than through ministerial instruments or policy incentives. A respondent in a very small municipality also pointed out that even here decisions were not made within local councils but within political parties, in that the ruling party required that party meetings must by rule precede a meeting of the municipal council in order to coordinate actions. This means that most decisions are taken in party meetings rather than by the individuals represented in municipal councils.

Yet another related effect is on suppressing inter-municipal cooperation. Respondents explained that a reason for a lack of cooperation is inter-mayoral competition for party attention. Cooperation reduces the chances that a particular initiative will be attributable to

an individual mayor – especially when smaller municipalities cooperate with larger ones – and in a political setting where visible attribution is important for rising through party ranks, joint initiatives make little strategic political sense. Politics also impacts the relationship between local self-governments and businesses. As one entrepreneur explained, ‘politics is a major issue for us. I’ve been in this for 20 years. In the first year of your work they [municipal staff] don’t trust you, then you start to cooperate and then you become serious partners, and then the government changes, and the whole process starts again. We are always seen as members of different parties, and have faced lots of opposition intermittently because of this, which slows down our work. The current government is now convinced of our work, but we expect that the next government will also not use our results and experience, and we will have to start again to build a better partnership’.

### *Trust Deficit*

Another related effect of the influence of politics within bureaucratic structures is a lack of transparency in decision-making, especially in decisions about what gets allocated to whom, and why. Many respondents pointed out that this may be responsible for the existence of a ‘trust deficit’ between citizens and the state. The implication is that citizens seem to think of the public service as operating to distribute discretionary benefits to certain groups, rather than the universal and non-discretionary distribution of services to all.

Respondents within Regional Development Agencies (RDA) pointed out that this also affects the business environment, determining which local enterprises receive municipal support and which do not. More worryingly for our purpose here, it means that even if the regulatory frameworks and capacities of local staff are strengthened, local businesses may not want to engage with the state. A stark example was provided by a local business in Niš, a co-working space that brings together a number of local entrepreneurs. In the interest of strengthening public-private partnerships, the company directors worked closely with the municipality to make a grant available to new entrepreneurs of about RSD five million. But few of these entrepreneurs were willing to take up the grants. The directors put this down to the trust deficit, suggesting that businesses did not trust that the money came without conditions, or that it would not embroil them in state processes in ways that would cause them to lose control at some point. This was despite the fact that the procedures for accessing the grant were not cumbersome. The money remains unused in large part to date, attributed to the past heavy-handedness of the state in Serbia, and to political interference in business activities.

Social trust between groups appears to be just as deficient. A number of respondents pointed out that local associations of farmers were very important for local producers in rural and remote parts to be able to engage with large businesses downstream in the value chain, and for large businesses to be willing to engage small upstream producers within their supply chains. Local economic associations reduce the transaction costs incurred by larger enterprises in finding upstream suppliers, and it enables local micro enterprises to find buyers, facilitate the requisite local infrastructure and raw materials, and negotiate with local self-governments. And yet, donors and state agencies have found it very difficult to induce such cooperation between local producers, attributed once again to the historical legacy of cooperatives in Serbia, and the arbitrary manner in which these were disbanded and disenfranchised in the 1990s and early 2000s. Interviews with various Chambers of

Commerce repeatedly underscored the value of having a single entity to bring together and coordinate many different producers. But respondents at Belgrade's Chamber of Commerce revealed that in trying to recently create an association of fruit producers through a donor project, they could not find ten producers from one area to agree to the establishment of an association. A respondent from a ministry revealed similar stories of having connected local farmers to buyers but had not been able to get them to work together to produce the quantity required.

### *Focus on equality rather than equity*

Within all this, both the formal rules as well as the way in which local self-governments function put little emphasis on special measures to enable access by vulnerable and marginalised groups, especially women and more remote populations. Most respondents across different tiers of government agree that this is important, but that the rules do not allow for this for the most intriguing of reasons — the fact that formal rules emphasise equality, which precludes any agency from being able to undertake affirmative action for women or other groups. This also applies to smaller versus larger municipalities (based on monotype local government units), and smaller versus larger businesses, all of whom are treated 'equally' under the law, usually through one size-fits-all measures and instruments. For example, the Ministry of Economy runs a Development Fund that provides financial support to new entrepreneurs, but the necessary documentation for applying to the Development Fund is quite complicated and small businesses and entrepreneurs need external support to prepare the application. Another example is that of the small business support programme for equipment procurement run by the Ministry of Economy and the Development Agency of Serbia, which sets minimum standards that are out of reach for small and micro businesses. The fact that the design of these initiatives has essentially excluded or priced out small and micro enterprises from access to available resources has not led to any changes in the way the modalities are designed, and the need for such changes is not currently part of the national narrative either.

Also, for business entities in difficulties, such as because of a reduction of employees or a reduction of cash flows, these support programmes are inaccessible. Such inaccessibility to available programmes, coupled with relatively high taxes, pushes many micro and family businesses into the zone of Serbia's already quite large grey economy. Given that 96.4 per cent of the SME sector consists of micro enterprises, that employ 47.6 per cent of employees in this sector,<sup>6</sup> this is an important consideration. According to the SME Report (2017), the largest fluctuations occur in this group, indicating frequent closures and re-opening, as well as business being conducted in the grey zone. Furthermore, there is no specially developed support system that prioritises businesses that function in less developed municipalities. The availability of funds is equal for all, so that businesses that operate in Western Serbia, Sumadija, South and East Serbia are dealt with under the same mechanisms as those in Belgrade and Vojvodina.

Needless to say, treating marginalised groups, areas or firms 'equally' usually leads to continuing unequal outcomes. Equitable outcomes require special measures instituted specifically to deal with the issues that marginalise specific groups so that their access to

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<sup>6</sup> Source: SME REPORT 2017, <https://privreda.gov.rs/publikacije/izvestaj-mspp-2017/>

services and resources can be enhanced and they can be included in development processes. In the case of LED, this would require special attention to the inclusion of women entrepreneurs, and to entrepreneurs from marginalised communities, such as the Roma, and from remote parts of the country that rarely get to participate in economic initiatives. Respondents agreed that women needed greater support and that they do not have equal conditions of employment or an equal economic playing field — there is a need for entrepreneurship training targeted at them; for greater support in writing project and grant proposals; and in dealing with municipal functions. However, according to the law on gender equality, such affirmative action would amount to discriminatory action against men. For example, a rulebook designed to improve the position of rural women by the Ministry of Agriculture — by supporting local associations of women who work on local crafts to support the expansion of rural tourism — was critiqued for exercising such discrimination since the actions were focused only on women. Respondents pointed out that unless national laws change, local governments cannot be expected to formulate instruments to focus on the specific needs of women in realising their economic potential in rural areas.

Youth is another group that is considered vulnerable because of a lack of employment opportunities, and their need to move away from their own regions in search of jobs and economic opportunities. However, this group is receiving more attention than others and there is a greater recognition of a need to focus on their needs in particular. This cannot yet be said for women entrepreneurs, or for Roma groups. Local self-governments do not have specific affirmative action programmes, and respondents suggested that this was not considered a priority area at either the national or local level. While there is a strategy for the inclusion of the Roma community, there is no obligation to have to implement it.

### *Solutions*

Current laws and political dynamics provide the context within which any intervention that seeks to strengthen the role of local self-governments in successfully achieving LED will need to be implemented. While the scope for donor-led change in this area is limited, there are a few possible solutions to the challenges outlined above. These include:

- Professionalisation of the service: Advocate for the reform of appraisal and reporting systems within the public services in order to increase accountability, reduce the impact of party politics, and increase the alignment between national plans, budgetary allocations, and actual implementation. The new law on planning systems can be used as the impetus for advocating for such change.
- Trust building and networked associations: Build specific trust building activities into programmes to enable communities to work with each other and with the state. Respondents suggested that this can be done by:
  - identifying and working with local champions who can work within their communities to change attitudes;
  - incentivising participation by making the benefits of participating in specific interventions and associations more explicit to communities (such as better and cheaper access to markets); and
  - through the development of long-term partnerships with strategic planning in which target communities can clearly see their own benefit.

Trust building in this way is important given that many respondents pointed out that networked associations of small producers are an absolutely essential part of kickstarting local economic development, especially in rural parts.

- Special focus on women and rural populations: Earmark a proportion of grants to target vulnerable groups such as women entrepreneurs, business activities in rural communities, and economic opportunities for youth groups. In doing this, it is important to provide detailed guidelines and templates to ensure that these groups can make full use of the opportunities, subsidies and support that are available to them in existing laws. Both financial resources and training are important, but in dealing with vulnerable groups, support is equally important. Respondents also suggested that guidelines and checklists should be designed for local self-governments to guide their work on LED, especially in terms of monitoring, tracking, reporting and analysing impact, and that these should emphasise the inclusion of and impact on vulnerable groups.

### **2.3. Actor Roles, Interests and Incentives**

In terms of the roles, interests and incentives of the main actors and stakeholders in initiating and implementing successful local economic development, the most prominent factors, in addition to those outlined above, are the following.

#### *Multiple actors, siloed functions*

As described earlier, the main issue with governance in Serbia is not a lack of 'institutional thickness', but one of coordination and coherence across multiple agencies and actors. The ministries that are most relevant to the subject of LED include: the Ministry of Economy, which defines national policies related to economic development; the Ministry of Public Administration and Local Self-Government, which has authority on public administration system at all levels, defines the system of local self-government, and leads on the education of public administration workers; the Ministry of Agriculture, Forestry and Water Management that is responsible for rural development and agricultural innovations; the Ministry of European Integration that is connected to regional development initiatives; the Ministry of Sports and Youth that looks at youth entrepreneurship and support to new companies; the Ministry of Trade, Tourism and Telecommunications, that has responsibility for investments in hospitality and for economic relations with foreign countries; the Ministry of Education, Science and Technological Development that supports investments in research and development; and the Ministry of Civil Engineering, Transport and Infrastructure, which has responsibility for spatial planning, urbanism, infrastructure projects, and measures associated with the 'ease of doing business' index.

There are then myriad other agencies and institutions that are also involved, such as the Development Fund run by the Ministry of Economy that provides loans to private enterprises; the Innovation Fund that is a grant scheme for innovative private sector start-ups; the Serbian Export Credit and Insurance Agency (AOFI) that provides support to exports; the Development Agency of Serbia (RAS) that incentivises, promotes and facilitates investments and provides support to SME programmes; the National Employment Service that collects and analyses data on unemployment and employment services; and a network of Accredited



Regional Development Agencies (RDAs) that are in charge of implementation of development policies at the regional level.

RDAs were envisaged as a particularly important actor, with their focus on regional development, coordination across municipalities, and SMEs in particular – all areas emphasised by the EU's accession instruments. RDAs are still considered an important stakeholder in LED, especially in terms of their relationship with multiple LSGs within specific regions, and their focus on building professional capacity within municipalities for applying for EU IPA funds. Despite some success stories of developing innovative projects, especially cross-border ones with neighbouring countries, respondents believe that the role of RDAs has not been as strong as originally envisaged. Local self-governments are founders of RDAs but their cooperation is occasional and focused largely around specific projects, an effect of an unclear legal framework for their cooperation and role. Respondents pointed out a number of issues with the way RDAs function – distance from many of the municipalities that they are responsible for; a lack of capacity to deal with their full jurisdiction; and focused, as a result, mainly on the main cities where they are based. Respondents in smaller municipalities could not recall having met or worked with RDA staff, and those in larger ones like Niš suggested that the capacity of the RDA was far below that required by larger centres and was largely dependent on the quality of individual leadership. Their role in facilitating inter-municipal cooperation has been particularly ineffective, but there seems to have been more success in bringing together local businesses within associations of producers.

Despite the existence of all these institutions, there is a sense that the subject of LED has slipped through the cracks that exist between the separated and siloed work of each of these. The fact that there was an insufficient level of coordination between institutional stakeholders at the central level formed a constant theme of our interviews. This was true despite the fact that LED is considered a subject of national priority, and was true even of the two main actors involved in this — the Ministry of Public Administration and Local Self Government (MoPALSG), and the Ministry of Economy (MoE). The former ministry (MoPALSG) considered the issue of economic development to lie outside its purview and firmly within that of the Ministry of Economy, while the latter (MoE) felt that the fact that primary responsibility for LED lies with local self-governments means that it has little to do with them and puts this subject firmly in the purview of the MoPALSG. Possibly because of this, many actors consider LED to be a donor-dependent sector, in that programmes work while donors are involved but that the incentives for sustainability are weak. This perception is closely connected to the historical origin and proliferation of LED offices across Serbia as part of a USAID-led initiative, and to the current precarious condition of these offices after the end of the programme, largely left to fend for themselves without any support from a central institution that takes ownership for LED.

#### *Lack of contact between LED offices and local businesses*

A major constraint on the successful implementation of local economic development is the lack of cooperation, and quite often even a complete lack of contact, between LED offices of local self-government and the local business sector. This was starkly visible even in small towns where the municipality, chamber of commerce, and many of the main local businesses are often located around the same square or park. Directors and other representatives of the local Chamber of Commerce and prominent business leaders sit on local government

committees and may attend meetings 2-3 times a year, but we were told that these are often formalised interactions and box-ticking exercises that are convened to meet legal obligations. There is little contact beyond this on a regular and informal basis that is organised around solving local economic problems.

Once again, this is not because of a lack of frameworks for such cooperation. There are three possible models for formal institutional collaboration of the business sector and local self-government according to the law. These are the Council for Economic Development; Local Employment Council; and the Social and Economic Council. The Council for Economic Development was established in almost all local self-governments in Serbia as an assembly body that brings together representatives from the public sector and the business and civic sector. However, the process of appointing members of the council is mostly non-transparent, and therefore the functioning of the Council has been reduced to formalistic interactions. The two other councils deal with issues of social development, collective bargaining, and employment, but they are not functional in most local self-governments. Despite the formal existence of these three institutional forms of cooperation, there is little interaction and communication in practice between the business sector and local LED offices.

#### *Weak capacity of local self-governments for LED*

A major constraint on local economic development is staff capacity at the local level in general, and within LED offices in particular. The generalised catch-all nature of these offices, political appointments of non-technical staff, and a recent ban on recruitment that has now lasted a few years, all mean that LED offices are severely under-staffed, and the staff that does exist are both over-burdened and have no specialised expertise on the subject of LED. Various respondents talked about this key constraint, but there was a real difference in the opinions of local and national actors. While local municipal staff in all types of cities and towns — from Group I all the way to those in ‘Devastated’ municipalities — pointed to this as a key reason for why they are unable to deliver on local economic development, national actors repeatedly suggested that the problem was not one of resources or staff, but of a lack of proper planning and prioritisation of objectives by local self-governments. This speaks to a real divide in the perception of local and national actors on this issue, with national actors deflecting responsibility for what they saw as strictly ‘local issues’.

Local actors, especially those in smaller and more rural municipalities, pointed out that they were affected by high levels of staff turnover because of low salaries and few job benefits that contribute to a brain drain to cities. At the same time, the ban on recruitment means that offices that were mandated to have up to six staff members in the LED office have only half that number dealing with all the prescribed functions. The overall implication of this for LED is that while national actors provide only broad and generalised one-size-fits-all prescriptions for local enterprises that need more customised business solutions, local LED offices have little capacity to provide these. As one LED officer in a small municipality pointed out, ‘we do not have capacity to visit businesses, let alone collect data on their needs and then process and analyse this to create specific instruments for them. We would need to visit 4-500 businesses a year, but how are three people supposed to do this?’ The issue of capacity and expertise did not improve in Group I and II cities either — technical knowledge and expertise

was still lacking, and as cities were bigger, so were the issues and number of businesses that a few LED office staff were dealing with.

Interestingly, this was also a reason mentioned for a lack of inter-municipal cooperation — ‘no one has excess capacity of staff to share responsibilities to make this happen’, said an LED official from a very small municipality facing multiple constraints that could be solved through coordination with neighbouring municipalities.

### *Solutions*

Issues such as those outlined above lend themselves more easily to programme interventions. Here are a few suggested solutions to these challenges:

- Inter-ministerial cooperation: Advocate for and incentivise the creation of inter-ministry groups on LED at the national level that can create greater horizontal coherence for work in this area. This is a key reform but given that it has strategic rather than visible value, it is not prioritised at present by policy actors.
- Capacity building of staff through training: Institute on-going professional development programmes that deliver regional training modules, a few times a year, to deal with access, mobility and staff retention issues. By developing short modules on the most important technical skills in the area of LED, municipalities can be assured of on-going access to skills training even if staff turnover remains high. And by delivering them regionally, these can be more easily accessed by all local staff. These training modules can be instituted through the recently constituted National Academy of Public Administration.
- Build monitoring and data analysis capacity within planning systems: Develop on-line guidelines for more effective and customised local planning systems that can prioritise key local needs. A key part of this is building capacity for and systems of effective and targeted data collection and analysis of the labour force and of local businesses, using minimal resources. There are weak monitoring mechanisms within the system and no culture of reporting on results. Current systems require reporting on inputs and outputs, rather than on outcomes and impact.
- Public sector reforms: Advocate for public sector reforms that can change the incentive structures within local governments and work to retain key staff members. Until recently, local government officials in Serbia were not regularised as public servants and did not have clear career development paths. The new Law on employees in autonomous provinces and units of local self-government (Official Gazette of the Republic of Serbia, No. 21/2016, 113/2017, 95/2018) now sets up a system of employment, professional development, monitoring and evaluation of work, as well as career advancement. However, the reform is not yet complete – the implementation of the Law on Salaries of Employees in Local Self-Government will start in 2020 – so that the environment in local self-governments continues to not be able to attract high-quality and competent staff.

## **2.4. Drivers and Constrainers of Change**

In summary, the main drivers and constrainers of change identified in the sections above are

the following.

### *Constrainers of change*

- Informal centralisation of governance through the use of political directives to local self-governments that works against the professionalisation of the service.
- Lack of institutional coherence and cooperation across multiple institutions, and siloed modes of operation, which reduce the extent of support available to under-resourced local self-governments.
- Lack of clarity on the formal role of local self-governments in local economic development, coupled with a severe lack of capacity to formulate local instruments and customised solutions for local businesses.
- Lack of integrated and comprehensive local development planning processes, and a lack of regularly updated data on the local economy and business needs, which works against the ability of local governments to provide better quality and more efficient support to local businesses.
- The ban on recruitment within the public service that restricts the extent to which local capacity can be improved and capacity of current offices expanded to deal with all of the functions listed above.
- A focus on equality, rather than on equity, which prevents affirmative action for the inclusion of women and minority group entrepreneurs, of rural or undeveloped municipalities, and of micro enterprises in national plans, instruments, and subsidy programmes.
- A trust deficit between state and citizens, and between communities, that reduces the extent of interaction and cooperation around LED activities.

### *Drivers of change*

- The new Law on Planning Systems provides for more integrated and comprehensive local planning for public policies that prioritises the production of public policy documents based on essential data collection, and on the results of ex-ante and ex-post analysis of impact. This includes a situation analysis; identification of envisaged change; development of measures and indicators of change for monitoring purposes; analysis of the expected effects and associated risks; and data collection for evaluating the impact of public policy. It also calls for consultations with stakeholders and target groups, and the need to collect and process different data in order to propose optimal solutions to local public policy issues.
- Amendments to the Law on Local Self-Government in 2018 (Article 88) have focused on inter-municipal cooperation. They encourage cooperation between multiple municipalities to form joint offices to which authority can be transferred for functions and processes that are originally the responsibility of individual local self-governments.
- Public sector reforms are on the national agenda, as evidenced by the new laws on planning, and there seems to be a recognition of the need to ensure greater accountability within the planning and implementation of public policy programmes.
- The establishment of the National Academy for Public Administration provides a unique opportunity to develop and institutionalise key training modules for the professional development of local public officials.
- The secretariat of public policy is working on the development of ICT systems for data

collection and analysis which is expected to correct the current data deficit within local government units.

- Amendments to the Law on Gender equality is currently under debate in parliament so that it can be used to develop affirmative action measures for women, especially those in rural areas that need extra support to be able to access development and economic opportunities and interventions.
- Measure of Active Employment Policy does actually focus on equity measures by focusing on 'hard to employ' groups, which includes women, people over 55 years of age, youth, and those with disabilities. The National Employment Agency is also working with municipalities to develop national and local action plans for employment, especially with regard to youth groups.
- An example of inter-ministerial cooperation has emerged at the national level with regard to economic opportunities for youth groups in the form of the National Inter-ministry commission on youth. This provides a useful precedent of coordinated engagement around issues of national importance.

### *Associated risks*

While there is a host of drivers that can be leveraged to move towards change, the risks associated with them remain the same as those that have affected most interventions, policies and laws to date in Serbia — the lack of implementation. The new Law on Planning is a great new opportunity, but as respondents pointed out, there is a chance that it will be approached once again as a box-ticking exercise, with municipalities borrowing from templates and other plans to quickly create their own development plans to meet legal obligations and deadlines. This is both because of a continuing lack of capacity and expertise that may not allow municipalities to make full use of this opportunity, but also because the law is overly complex with few guidelines on making the most effective use of its provisions.

Respondents also pointed out that the problem in Serbia has never been one of a lack of laws and policies, but one of implementation, and specifically, of monitoring implementation. As one respondent asked, 'who is looking at the monitoring, and who is monitoring the monitors? And what are the sanctions for those not complying?' Another added, 'plans do exist, it is inclusive implementation and monitoring and accountability that does not. This is what has always been missing. Institutions and frameworks exist, but no one is holding anyone accountable to these.' At the heart of this, of course, lies the nature of the local public service, with its lack of capacity and expertise; inability to ensure compliance with laws and regulations because of politically motivated appointments; and the practice of hiring through political patronage rather than career track appointments.

### 3 From solutions to intervention

Most of our respondents agreed that this was the right time to work on the subject of local economic development. It is important on the national agenda, and fits well within Serbia's strategic development policy goals, as outlined in the 'National priorities for international assistance in the Republic of Serbia 2014-2017, with projections until 2020 (NAD)' policy document.<sup>7</sup> It also links to policy objectives outlined in a number of other national priorities – Public administration reform strategy in the Republic of Serbia 2018-2020; National strategy for young people 2018-2020; Strategy for support of SME development and competitiveness for the period from 2015 to 2020; and the laws on local self-government and on the planning system of the Republic of Serbia. Work on LED has the potential to advance Serbia's strategic development priorities in reforming the public services to create an efficient and effective public administration; stimulating economic growth and improvement across the country to increase national and regional prosperity; and strengthen social protection of the most vulnerable social groups. These strategies envisage a central role for local self-governments in Belgrade, the 23 towns and 150 municipalities. Some of the most important processes in this regard are: enhancement of efficiency and effectiveness of public administration; professionalisation of public administration; improvement of strategic planning and coordination of public policies; improvement of public finance management, especially integration of strategic planning with the budget process; strategic framework for public finance management and strengthening transparency and accountability of public administration.

Local economic development is also significant for Serbia's EU accession process and meets the need for systematic reforms to achieve socio-economic development according to the Copenhagen criteria. The EU's IPA thematic priorities (focused around accession) emphasise promoting employment, labour mobility and social inclusion; improving public infrastructures; promoting local and regional governance, planning and administrative capacity building; and enhancing competitiveness, business and SME development, trade and investment. Developing local enterprise in line with these priorities is a major area of work for the Ministry for European Integration.

A particular priority of the current government is the reduction of unemployment, primarily through the development of entrepreneurship and small and medium enterprises.<sup>8</sup> In policy documents of the government, as well as in the SME Development Strategy, special attention is paid to models of support to small and medium-sized enterprises, as well as to local economic development, with particular emphasis on EU requirements around inclusive development focused on the needs of marginalised groups in smaller municipalities.

Overall, the subject of local economic development is emphasised across a number of policy objectives, but this has so far been in terms of discourse only without coherent and effective action plans on how to achieve this, especially in areas where it might be most needed – in small and rural communities across the country. Many of our respondents pointed out that small, rural municipalities are the norm in Serbia and should be the focus of new

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<sup>7</sup> [http://www.evropa.gov.rs/Documents/Home/DACU/12/74/NAD%202014-2017%20with%20projections%20until%202020%20\(english\).pdf](http://www.evropa.gov.rs/Documents/Home/DACU/12/74/NAD%202014-2017%20with%20projections%20until%202020%20(english).pdf)

<sup>8</sup> [https://media.srbija.gov.rs/medsrp/dokumenti/ekspoze-mandatarke-ane-brnabic280617\\_cyr.pdf](https://media.srbija.gov.rs/medsrp/dokumenti/ekspoze-mandatarke-ane-brnabic280617_cyr.pdf)

programmes in this area. Besides the fact that such municipalities represent the majority, another reason for focusing on them is connected to the need to reverse the trend of depopulation of rural areas. This occurs through the migration of younger population groups in particular to Serbia's towns and cities in search of employment. By enhancing economic opportunities in small and rural municipalities, LED focused interventions can significantly contribute to reducing such depopulation.

Many businesses in small and rural municipalities are micro enterprises (MEs). As stated earlier, MEs make up more than 90 per cent of the SME sector and employ almost half of the workforce in this sector. Yet, MEs are particularly disadvantaged compared to other business sectors – they have difficulties in accessing subsidised sources of funding, face a regressive tax regime that disincentivises their work, and have a relatively high administrative burden given their small size. This forces many of them into the grey zone of the economy in order to survive. Focusing on MEs in enhancing local economic development is in line with recent efforts to reduce the size of the grey economy in Serbia, outlined in the 'National programme for the suppression of grey economy for the period 2019-2020'. Together with envisaging changes in tax policy and inspection activities, this policy also includes support measures for small and new businesses and for improving the business climate for the ME sector in particular.

### **3.1. Components of an Intervention**

In designing an intervention to strengthen local economic development, many of the solutions our respondents suggested focused on resolving coordination issues at various levels, in particular:

- a. Between municipalities;
- b. Between local self-governments and the private sector;
- c. Between local businesses;
- d. Between local and national governance.

We detail below specific coordination issues and suggestions for resolving these at each of these levels, and then connect these solutions to some suggested interventions at the end of this section.

#### *a. Inter-municipal cooperation*

Respondents agreed both on the need for inter-municipal cooperation and the role that RDAs can play in this, but insisted that institutional and legal coherence was missing at the national and regional level so that responsibility for achieving such cooperation came down largely to individual municipalities. A strong suggestion for a workable solution made by the LED team in Niš was to create a regional structure, possibly through legal frameworks, that demarcated up to 80 kms around larger towns and cities with the specific purpose of connecting municipalities around common economic objectives or particular sectors – in other words, sector level inter-municipal cooperation across 'functional regions'. This would require LSGs in proximate regions working together to cluster entrepreneurs within identified sectors for support, networked cooperation, and training. This could possibly be done under

the Serbian Development Agency, possibly in collaboration with RDAs, with the specific aim to identify, facilitate and boost regional cooperation initiatives. In areas without a proximate urban centre, this could be done to bring together smaller municipalities.

The need to include larger urban centres to cooperate with smaller municipalities was underscored by a number of respondents. While conceding that this could sometimes threaten smaller municipalities, they believed that overall this could promise benefits that accrue from spillover effects from urban centres that may not be able to fully absorb economic activities, or may need support from smaller, more rural municipalities for specific reasons. For example, the urban centre of Niš no longer has enough industrial land to offer to investors, and especially not at affordable prices, while smaller, rural municipalities have plenty of land at low prices but no investors (land prices compare at €50 per square metre in Niš to about €2-3 per square metre in the surrounding areas). Partnerships between municipalities can ensure that investors can be moved out to more rural settings without urban centres sacrificing all revenue in the process. Furthermore, in Niš's bid to become a tourist centre, it needs the cooperation of rural municipalities to create full itineraries for visitors that include opportunities for rural and adventure tourism, spas and natural trails and sights. Smaller municipalities like Bojnik also suggested that such cooperation could work well, but smaller municipalities would need protection through legal frameworks to avoid being swallowed up or overshadowed within such agreements, and to ensure that proportionate credit accrues to the mayor and LED office of each participating municipality. This is now on both the SCTM and the secretary for tourism's agenda.

In designing an intervention, respondents strongly suggested that the proposed programme should bring together local self-governments with national level actors to create innovative inter-municipal cooperation practices that can then act as a model for other municipalities. Such benchmarks of successful practice – of successfully translating national priorities into localised solutions by working together – are missing at present and can be a major contribution to the programme. They insisted that this should work through a set of 'pilot municipalities', to which municipalities must apply, rather than being selected into the programme. Such horizontal and vertical coordination, some suggested, 'would be a real test of our maturity' and would provide reference points and examples for other municipalities to follow.

#### *b. Stronger interaction between LSGs and private sector*

To deal with the lack of institutionalised contact between LSG LED offices and local businesses, respondents overwhelmingly suggested that the main solution was for LSGs to play a decisive role in creating associations of local businesses that could pool their resources for both production, information sharing, and access to markets. Respondents provided the example of Kruševac's innovation centre that was established by the municipality, and suggested that local businesses can benefit greatly from the creation of co-working spaces for local business focused on locally inspired innovations. In doing so, LSGs should focus in particular on MEs that require support in terms of project writing to apply for development funds available nationally.

This of course requires that LED staff develop the capacities, tools and templates to be able to do this. The trend so far is to connect with the most proximate and visible businesses, and



not smaller enterprises that might require far more support. It also requires stability across teams that work with small businesses, since much of this comes down to developing personal linkages between staff and local producers and developing detailed knowledge of procedures through experience. The LED team in Niš emphasised the fact that their particular success comes from a team that has been in place for about ten years now. Furthermore, it requires that LSGs have more complete data on SMEs in their area, and then based on this, design and develop specific instruments for SMEs and ensure that these are implemented. This was an approach advocated by the Ministry of Economy.

Another specific area of intervention is to develop frameworks for results-based management within LED offices. Reporting on results at the moment focuses on inputs and outputs, rather than on outcomes and impact. Similarly, accountability structures in terms of results do not exist. SCTM developed some indicators in the area of LED for a sample of 50 municipalities, and these can be built on further. In terms of building capacity, respondents mentioned a few specific areas on which training was required in particular:

- What LED actually entails and the different models that local self-governments can choose from.
- How to create and facilitate networks and associations of local businesses, especially those inclusive of women, youth and marginalised groups.
- Leadership and decision-making.
- Results-based management, and monitoring, learning and evaluation (MLE) frameworks.
- More advanced modules around public procurement, industrial zone management, incentivising growth, creating innovative local instruments that are area specific, and so on.

From the perspective of local businesses, the main areas of cooperation suggested were: better and more flexible state subsidies; better and more open communication so that MEs know who to go to for specific things; and more stable linkages that are built on relationships of trust – because ‘we generally are made to feel like we are working against government’ said one entrepreneur. Local businesses repeatedly pointed out that they wanted more space within key decision-making bodies, more functional local business councils, and meetings that were not box-ticking exercises and whose decisions are actually implemented as action points. This was not necessarily vis-à-vis international opportunities but simply national ones – ‘for SMEs, the real goal is getting to Belgrade. Exports are not really the main thing on their agenda’, explained one member of a Chamber of Commerce. Business actors admitted to the centrality of local government involvement, in particular for MEs, and especially in terms of the provision of space, local infrastructure, support in accessing markets and finance, and for basic information on regulations, by-laws and registration procedures. Some requests were simply for more updated information available on municipal web sites.

A major suggestion was focused on the role that public procurement could play in stimulating local businesses. The total value of public procurement each year is very large (‘more than the value of all health care sector’, according to an analysis by the Belgrade Chamber of Commerce) and this in itself could provide a major market for local produce if local content use was encouraged. Many LSGs already use this instrument to incentivise SMEs, and this

could be used further to develop regular market mechanisms and instruments to achieve sustainable goals locally. Public procurement can be used to empower women entrepreneurs by inviting women in particular to bid for contracts and apply to projects, and prioritising the selection of local firms that meet minimum standards and are led by women.

*c. Coordination between local businesses:*

Most respondents from both the private and public sector were unanimous in the need for LED to focus in particular on the needs of MEs, and for these to work together through local business associations. The main need of small businesses is finding markets for their products, and the creation of associations of producers can enable larger pools of knowledge, information and experts that help small producers get their produce to larger markets. They can also work to link up producers at different levels to bring together different parts of the value chain. LSGs and Chambers of Commerce can work together with these associations to engage experts on market access and also attract larger investors because greater quantities can be assured. Many respondents pointed to the fact that a lack of such associations has meant that individual businesses try and find investors and buyers on their own, often with little success. Respondents provided various examples of well-funded programmes that have failed in the past because of a lack of networks, associations and cooperation across individual producers.

Co-working spaces focused on finding innovative solutions for local problems were particularly popular suggestions made by our respondents, especially in providing supportive spaces for women entrepreneurs, and for engaging both younger and older populations. They pointed out that such associative spaces were fully sustainable in bigger cities, but in smaller municipalities an initial subsidy could really help in getting them started. Respondents suggested that the proposed intervention could create 2-3 associations of businesses, or Local Action Groups (LAGs), from participating municipalities to work together towards developing a joint strategy and apply to calls, especially those of the EU that encouraged such a collective approach. This could work very well with the suggestion for inter-municipal cooperation across sector-based 'functional regions' made above.

*d. Coordination between local and national governance*

Coordination and engagement between local and national governments, and between public and private sectors at all levels is very weak. Most actors admitted that rather than lobbying for better linkages and required changes, most actors on both sides have just tried to get on with things on their own – state institutions do not provide private actors a voice in decision making fora, and private actors do not engage with the public sector in lobbying for or supporting required changes. Respondents agreed that there was a need to better link up national and local levels but that this was not a particularly functional aspect of governance at present. Most governance was top-down, centralised and rigid, and while policies and frameworks flowed downwards from the centre, little flowed upwards in terms of the bottom-up setting of priorities. For example, on rural policy, LSGs are very inactive on designing clear local policies that provide customised solutions on local development and agricultural development. All local policies look like national policies and replicate national priorities and interests, instead of designing interventions that address their own particular needs. This is

particularly true in the area of finance, where generalised finance instruments are used rather than those customised to specific areas and sectors.

Respondents believed that the national level had a particularly important role to play in improving coordination between the public and private sectors by strengthening legal frameworks and the pool of expertise available for this, and for creating incentives and lines of responsibility around the creation of local, customised solutions. A good example of this was the partnership between national and local levels around the National Action Plan for Employment under which local priorities around public employment and public works are coordinated with the national plan.

Respondents also stressed the need for spaces for policy dialogue across the multiple national ministries, and between national and local governments that is focused on removing bottlenecks, undoing clogs in the system, and making useful connections. Such dialogue is not a natural or organic occurrence and must be developed as a specific component of the proposed intervention

### 3.2. Matching Solutions to Suggested Interventions

Most suggested solutions centred repeatedly on a few key interventions – strategic planning and building capacity and knowledge for this; strengthening accountability; creating local associations of businesses to enable micro enterprises; building networks that bring local self-governments and businesses closer in creating procedures and instruments that enable local enterprise; strengthening inclusion of marginalised groups; and working on vertical linkages and public sector reforms. These are detailed in the table below which connects the solutions presented in Sections 2.1 to 2.3 to proposed interventions that can implement these.

AREA	SOLUTIONS	INTERVENTIONS
1 <b>Strategic planning</b>	Flexible, but functional, planning at the local level that is customised to the needs of the local economy and businesses.	Work with the implementation of the new Law on Planning Systems
		Build technical capacity of LSGs to create clearer instruments that work for local businesses, and to provide technical support on these instruments to local businesses.
		Work with the implementation of the regulation on content, method of preparation, evaluation and monitoring, and reporting on realisation of capital projects
		Simple guidelines (on shared websites) for planning and prioritisation (connected to data collection and analysis below)
	Develop planning systems and guidelines to help develop capacity within the system for strategic planning (sustainability) and prioritisation	Simple guidelines (on shared websites) for customising plans to local needs

of needs

	Systems of data collection and analysis -- regular and updated to enable needs prioritisation and effective use of resources	Build capacity around minimal and basic data collection on local economy and business needs (connect to data needs in other sectors to build holistic capacity) Develop interactive online tools on municipal web sites for this
<b>2 Capacity building</b>	Institute on-going professional development programmes that deliver regional training modules	On-going training programmes (delivered regionally, a few times a year, to deal with mobility and staff retention issues), possibly developed with and hosted by National Academy for Public Administration
<b>3 Enabling MEs</b>	Adaptive environment created by LSGs to enable MEs through support on local and national frameworks that apply to these, especially those led by women, youth, and in rural or undeveloped areas	Process review to figure out most pernicious bottlenecks and the processes that MEs find most difficult to deal with Develop guidelines for LSG staff on how to make these processes easier, quicker, less complex for local businesses Incentivise participation through assistance, such as: exemption from the payment of certain local taxes, the granting of public property for use free of charge or at lower than market rates, cash benefits, subsidies for job creation, procurement of equipment
	Facilitate associations and trust building between LSGs and local businesses	Develop activities and conversations between LSGs and local businesses through this process that can increase the trust between them and make benefits more explicit Encourage the creation of associations, and identify and work with change champions that can work with local entrepreneurs and producers, especially in rural areas
<b>4 Strengthening inclusion and reducing de-population</b>	Special focus on women and rural populations to improve equity of outcomes, and on youth to reduce de-population and migration	Develop the guidelines, strategic plans and data collection tools to deal specifically with these groups

	Make localised plans that can create customised solutions for the prioritised needs of these groups, and for:	See above
	small municipalities vs. larger; small firms vs. larger	Policy dialogue -- advocacy to ensure that calls put out by ministries focus on the needs of MEs and of smaller LSGs (empowering those that fall outside the national nets)
<b>5 Coordination and linkages with national institutions, and national ownership of reforms</b>	Advocate for and incentivise the creation of inter-ministry groups on LED at the national level that can create greater horizontal coherence for work in this area.	Policy dialogue focused on inter-ministerial dialogue (horizontal linkages through careful composition of group); and ministry-local government linkages (vertical linkages through emphasis on this in group)
	Incentivise inter-municipal cooperation to bring two or more municipalities together in developing common local economic programmes and development plans.	Incentivise inter-municipal cooperation by building it into the technical assistance and grants modality
		Link up inter-municipal cooperation with associations of local businesses (rural hubs, co-working spaces), either existing ones or create new ones through the programme
<b>6 Public sector reforms</b>	Professionalisation of the service, and reform of the appraisal and reporting systems, connected to the new law on planning to increase accountability	Advocate for the importance of these changes through the policy dialogue group, and maybe through demonstrating best practices in some key municipalities. Use the new Law on Planning as the impetus to advocate for such change
	Advocate for public sector reforms that can change the incentive structures within local governments and work to retain key staff members, such as regularisation and career development paths	Advocate for the importance of these changes through the policy dialogue group

# Annex I

This report is based on data collected through semi-structured interviews with 51 respondents in the following institutions:

## **Municipalities**

- City of Leskovac
- City of Niš
- City of Kruševac
- Municipality of Bojnik
- Municipality of Aleksinac
- Municipality of Trstenik

## **Private sector**

- Chamber of Commerce of Serbia
- Chamber of Commerce Belgrade
- Regional Chamber of Commerce, Niš
- Regional Chamber of Commerce, Leskovac
- Regional Chamber of Commerce, Kruševac
- DELI - coworking space, Niš
- StartUp Centre, Niš
- TS Alatnica, Trstenik
- Entrepreneurs Association Trstenik
- Danko.d.o.o, Trstenik (Limited liability company)
- 'Jugogradnja' d.o.o, Bojnik (Limited liability company)

## **National-level institutions**

- Ministry for Public Administration and Local Self Government
- Ministry for Economy
- Ministry for EU Integration
- Ministry for Agriculture, Woods and Water Management
- NALED, National Alliance for Local Economic Development
- SCTM, Standing Conference of Towns and Municipalities

## **Regional Development Agencies**

- Center for Development Jablanica and Pcinja Districts
- ARRRO d.o.o, Agency for Regional Development of Rasina District

## **Other**

- Independent Consultant